

Sarla Performance Fibers

Textile

Result Update

4 June 2018

Nylon66 to boost revenues from FY20E

We maintain our BUY on Sarla Performance Fibers with a revised TP of Rs67 as we value the company based on our conservative adj. OCF based methodology. We expect the domestic volumes to grow by high single digit on the back of increasing capacity in the industrial/performance yarn segment by 700MT while the Nylon66 capacity would be increased to 1600MT from H2FY19. Further the company could take marginal price hikes to mitigate the impact of increase in RM prices. Operating loss of Sarla Flex to reduce to Rs45mn in FY19E from Rs104mn in FY18 would add to margins. Lower debt, improving working capital further gives us comfort while valuations continue to remain undemanding.

- **Q4FY18 result highlights:** Consolidated sales was down 10% YoY to Rs729mn while standalone sales declined by 2.5% YoY to Rs686mn. Lower duty drawback, decline in wind power sales coupled with closure of Sarla Flex impacted revenue growth. Operating profit was at Rs82mn against loss of Rs2mn last year for the company. Sarla Flex posted operating loss of Rs66mn on revenue of mere Rs10mn. Gross margin was down 386bps to 42.4% while operating margins was mere 11.2%. PAT loss was Rs42mn on the back of higher taxes in Sarla Flex while in the standalone company PAT was at Rs36mn against Rs70mn in Q4FY17.
- **Increase in domestic capacity to boost sales:** Domestic capacity has been increased by 700MT in the month of April'18 which would increase the installed capacity to 13.6K MT. Further the company is increasing the Nylon 66 plant to 1600MT from current 450MT. We believe the benefits of Nylon66 plant would come from Q4FY19 as company had more than 50% capacity utilisation in FY18 and garnered sales of Rs68mn which we believe would increase to Rs343mn in FY20E. We believe the company has strong order book from the domestic clients and is confident of near double digit volume growth while the pricing growth would be low single digit. During FY18 company had 0.9% volume growth while pricing growth was 6% in the core yarn business. However we believe with the increase in commodity prices, RM prices are on an uptick with chip prices increasing by 23% in FY18.
- **Sarla Flex to have operating loss of ~Rs45mn in FY19E:** In FY18 Sarla Flex garnered revenue of Rs133mn with EBITDA loss of Rs104mn and PAT loss of Rs172mn. However from FY19E onwards we have modelled revenue of mere Rs3mn while EBITDA loss of Rs45mn as the company has to pay property tax and marginal other expenses and less than Rs9mn employee cost. While PAT loss for FY19E would be Rs92mn on Rs70mn depreciation, cash loss would be Rs25mn as the company would also have other income of Rs30mn. We believe the management continues to find customers for the plant and till then the plant would continue to remain closed.
- **Maintain BUY:** We have lowered our revenue by 2.6% for FY19 on lower domestic sales while increased the same by 3.3% for FY20E on increasing capacity utilisation for Nylon66. Operating profit has been cut 24.7%/23.3% for FY19E/FY20E on lower gross margins and increasing loss in Sarla Flex while PAT has been cut by 29.2%/27.2% over same time. We maintain our BUY on Sarla Performance Fibres with a TP of Rs67 as we value it on adjusted OCF (AOCF = OCF – Interest) to enterprise value (EV) yield. Key risks being increasing pressure on RM prices lowering gross margins.

Y/E Mar (Rsmn)	Q4FY18	Q4FY17	YoY (%)	Q3FY18	QoQ (%)	Q4FY18E	Var (%)
Net Sales	729	811	(10.2)	764	(4.7)	756	(3.6)
COGS	420	436	(3.7)	361	16.3	370	13.4
Employee Expenses	26	74	(64.6)	32	(19.1)	33	(21.0)
Admin & Other Exp	201	304	(33.8)	186	8.0	200	0.7
EBITDA	82	(2)	NM	185	(55.9)	153	(46.8)
EBITDA margin (%)	11.2	(0.3)	1,148bps	24.2	(1,297)bps	20.3	(906)bps
Depreciation & Amm.	58	58		48		50	
Other Income	24	130		32		35	
Interest	17	21		16		17	
PBT	29	48	(39.5)	152	(80.8)	121	(75.9)
Tax	72	56		51		35	
Adjusted PAT	(42)	(8)	NM	101	NM	86	NM

Source: Company, Centrum Research

Y/E Mar (Rs.mn)	Revenue	YoY (%)	EBITDA	EBITDA (%)	Adj PAT	YoY %	Fully DEPS	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY16	2,977	(4.6)	597	20.0	450	61.2	5.4	18.3	9.5	10.2	8.9
FY17	3,033	1.9	494	16.3	411	(8.8)	4.9	14.8	8.2	8.7	12.8
FY18	3,025	(0.2)	548	18.1	240	(41.5)	2.9	8.2	5.4	14.9	10.0
FY19E	3,176	5.0	624	19.6	385	60.2	4.6	12.7	8.0	9.3	6.8
FY20E	3,584	12.8	687	19.2	442	14.9	5.3	13.4	8.7	8.1	5.8

Source: Company, Centrum Research Estimates

In the interest of timeliness, this document is not edited

Centrum Equity Research is available on Bloomberg, Thomson Reuters and FactSet

Target Price	Rs67	Key Data	
CMP*	Rs43	Bloomberg Code	SRPL IN
Upside	56%	Curr Shares O/S (mn)	83.5
Previous Target	Rs100	Diluted Shares O/S(mn)	83.5
Previous Rating	Buy	Mkt Cap (Rsbn/USDmn)	3.6/54.4
Price Performance (%)*	52 Wk H / L (Rs)		82.6/41.5
	1M	6M	1Yr
SRPL IN	(14.6)	(23.9)	(22.3)
Nifty	0.7	2.2	10.7
		5 Year H / L (Rs)	91.5/15.5
		Daily Vol. (3M NSE Avg.)	97602

*as on 4 June2018; Source: Bloomberg, Centrum Research

Shareholding pattern (%)*

	Mar-18	Dec-17	Sep-17	Jun-17
Promoter	54.6	55.2	55.5	55.4
FIs	0.0	0.0	0.0	1.1
DIs	5.9	5.9	9.3	13.9
Others	39.5	38.9	35.2	29.6

Source: BSE, *as on 4 June 2018

Earning Revision

Particulars (Rs bn)	FY19E			FY20E		
	New	Old	Chg (%)	New	Old	Chg (%)
Sales	3,176	3,259	(2.6)	3,584	3,468	3.3
EBITDA	624	828	(24.7)	687	896	(23.3)
EBITDA margin (%)	19.6	25.4	(577)bps	19.2	25.8	(665)bps
Adj PAT	385	544	(29.2)	442	607	(27.2)

Source: Centrum Research estimates

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Valuation

We value SPFL on AOCF/EV yield methodology and arrive at a target AOCF/EV yield of 6.7% for SPFL, and hence, the implied EV/AOCF multiple of 12.4x post giving a 20% discount. We use average cash flows generated over five years (and hence remain conservative) during FY16-20E and apply 12.4x multiple to arrive at our target EV and our TP of Rs67. Reiterate Buy. At our TP of Rs67, stock would trade at FY19E/20E P/E of 14.5x/12.6x.

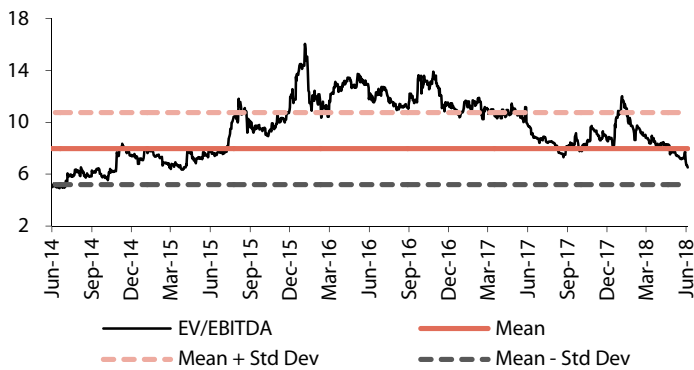
Exhibit 1: Cash Flow based Valuation

5 Year average Adj. OCF Yield (AOCF/EV) - % (FY14-18E)	6.7
Discount	20.0%
Implied EV/AOCF Multiple (x)	12.4
Average Adj. OCF (Rs mn) - FY16-20E	486
Target EV (Rs mn)	6041
Less: Net debt (FY20E)	427
Target market cap (Rs mn)	5614
No. of shares (mn)	83.50

Target Price/share (Rs) 67

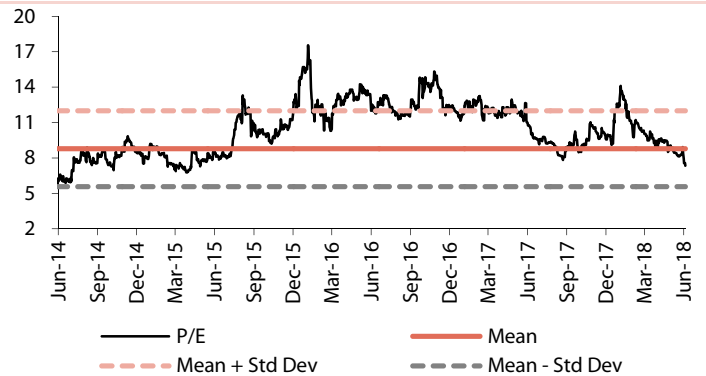
Source: Company, Centrum Research Estimates

Exhibit 2: 1 year forward EV/EBITDA chart



Source: Bloomberg, Company, Centrum Research Estimates

Exhibit 3: 1 year forward P/E chart



Source: Bloomberg, Company, Centrum Research Estimates

Exhibit 4: Comparative Valuations

Company	Mkt Cap (Rsmn)	CAGR FY17-FY19E (%)			EBITDA Margin (%)			PE (x)			EV/EBITDA (x)			RoE (%)			Div Yield (%)		
		Rev.	EBITDA	PAT	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E
Sarla*	3,649	8.8	11.9	35.7	18.1	19.6	19.2	14.9	9.3	8.1	10.0	6.8	5.8	8.2	12.7	13.4	2.0	2.8	3.0
Vardhman Textiles	71,361	6.7	19.9	22.3	14.8	17.9	18.7	11.6	9.1	7.9	8.7	6.9	6.0	12.7	13.8	14.2	1.2	1.5	1.7
Welspun India	62,042	8.3	9.8	18.2	19.8	19.6	20.3	17.4	12.5	10.5	8.6	6.8	5.9	18.6	19.0	18.5	1.5	1.9	2.2
KPR Mill	44,182	8.8	10.0	14.4	19.7	19.9	20.1	18.5	12.6	11.1	10.6	7.4	6.7	20.6	19.3	19.0			
Himatsingka Seide	34,327	13.5	24.8	27.2	19.8	21.9	24.0	16.7	12.9	10.2	10.1	9.1	7.5	17.0	18.7	20.1	0.9	0.9	1.4
Indo Count Industries	14,854	6.5	10.3	9.1	13.7	14.2	14.7	16.7	8.9	7.8	10.7	6.1	5.4	16.9	15.5	15.2	0.5	1.1	1.1
Global Peer																			
Unifi Inc#	592	4.7	20.2	23.9	7.2	8.8	9.4	31.4		16.1	12.4	9.5	9.7	11.8	11.8	9.0	0.0	0.0	0.0

Source: Bloomberg consensus, Companies; *Centrum Research Estimates; #Mcap in USD mn, June End

Quarterly financials, Operating Metrics and Key Performance Indicators

Exhibit 5: Quarterly Financials

Particulars (Rsmn)	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18
Total Income	750	790	724	811	791	746	764	729
COGS	312	279	291	436	369	359	361	420
Employees expenses	53	62	54	74	53	53	32	26
Other expenses	200	261	218	304	211	209	186	201
Total Expenditure	565	603	563	814	633	621	580	647
EBITDA	185	187	161	(2)	157	125	185	82
Depreciation	45	46	48	58	51	44	48	58
EBIT	140	142	113	(61)	106	81	137	23
Interest	32	20	13	21	22	18	16	17
Other Income	37	55	53	130	42	82	32	24
Exceptional Items	0	0	1	1	1	1	1	1
PBT	146	177	153	48	127	144	152	29
Total tax	54	39	41	56	36	53	51	72
Reported PAT	91	138	112	(8)	91	91	101	(42)
Adj PAT	91	138	112	(8)	91	91	101	(42)
Growth %								
Revenue	(6.2)	(3.2)	(1.9)	15.8	5.4	(5.6)	5.6	(10.2)
EBITDA	7.3	(7.7)	(7.4)	(103.6)	(14.9)	(33.5)	14.8	NM
PAT	(9.0)	4.2	(25.5)	(111.9)	(0.9)	(33.6)	(9.5)	419.1
Margins%								
Gross Margin	58.4	64.7	59.7	46.3	53.3	51.8	52.8	42.4
EBITDA	24.7	23.7	22.2	(0.3)	19.9	16.7	24.2	11.2
EBIT	18.7	17.9	15.5	(7.5)	13.5	10.8	17.9	3.2
Adj PAT	12.2	17.4	15.5	(1.0)	11.5	12.2	13.3	(5.8)

Source: Company, Centrum Research

Financials

Exhibit 6: Income Statement

Y/E March (Rs.mn)	FY16	FY17	FY18	FY19E	FY20E
Revenue	2,977	3,033	3,025	3,176	3,584
Employee Cost	215	242	164	125	134
%of revenue	7.2	8.0	5.4	4.0	3.7
Material cost	1,224	1,309	1,509	1,587	1,799
%of revenue	41.1	43.2	49.9	50.0	50.2
Other expenses	940	988	804	840	964
% of revenue	31.6	32.6	26.6	26.4	26.9
EBIDTA	597	494	548	624	687
EBIDTA Margins (%)	20.0	16.3	18.1	19.6	19.2
Depreciation & Amortization	155	178	202	212	227
EBIT	442	315	347	412	460
Interest expenses	65	71	74	58	55
PBT for operations	377	244	272	354	406
Other income	131	318	180	195	215
Exceptional item					
PBT	508	562	452	549	621
taxes	57	149	211	164	178
Effective tax rate (%)	11.1	26.6	46.7	29.9	28.8
Net Profit	451	412	241	385	442
Minority interest/associates	(1)	(2)	(1)	0	0
Adj Net Profit	450	411	240	385	442

Source: Company, Centrum Research Estimates

Exhibit 7: Key Ratios

Y/E March	FY16	FY17	FY18	FY19E	FY20E
Growth ratios (%)					
Revenues	(4.6)	1.9	(0.2)	5.0	12.8
EBIDTA	20.3	(17.3)	11.1	13.7	10.2
Adj Net Profit	61.2	(8.8)	(41.5)	60.2	14.9
Margin ratios (%)					
EBIDTA Margins	20.0	16.3	18.1	19.6	19.2
PBT from operations	12.7	8.0	9.0	11.1	11.3
PAT Margins	15.1	13.5	7.9	12.1	12.3
Return Ratios (%)					
ROCE	9.5	8.2	5.4	8.0	8.7
RoNW	18.3	14.8	8.2	12.7	13.4
RoIC	15.5	8.9	7.5	10.8	11.8
Turnover Ratios (Days)					
Gross Block turnover(x)	1.04	0.89	0.80	0.83	0.89
Inventory period	113.6	94.6	71.9	75.0	75.0
Collection period	95.6	114.9	95.7	100.0	100.0
Payment period	18.9	18.5	15.3	15.0	15.0
Cash conversion cycle	190	191	152	160	160
Solvency Ratio					
Debt-equity	1.0	0.9	0.7	0.6	0.5
Net Debt-equity	0.3	0.3	0.3	0.2	0.1
Current ratio	4.7	3.5	4.3	4.5	4.5
Interest coverage ratio	6.8	4.4	4.7	7.1	8.4
Gross debt/EBITDA	4.5	5.3	3.7	3.1	2.7
Per Share (Rs)					
FDEPS (Adjusted)	5.4	4.9	2.9	4.6	5.3
CEPS	7.2	7.1	5.3	7.1	8.0
Book Value	31.4	35.2	34.6	37.8	41.5
Dividend per share	1.1	1.1	1.1	1.2	1.3
Dividend Payout (%)	23.3	26.8	45.9	31.2	29.5
Valuations (x)					
PER	10.2	8.7	14.9	9.3	8.1
P/BV	1.8	1.2	1.2	1.1	1.0
EV/EBIDTA	8.9	12.8	10.0	6.8	5.8
5 Yrs avg AOCF/EV Yield (%)	4.5	6.4	7.7	9.8	12.1
Dividend yield (%)	1.9	1.7	2.0	2.8	3.0

Source: Company, Centrum Research Estimates

Exhibit 8: Balance Sheet

Y/E March (Rs.mn)	FY16	FY17	FY18	FY19E	FY20E
Share Capital	84	84	84	84	84
Reserves & Surplus	2,536	2,854	2,808	3,073	3,385
Total Shareholders Funds	2,619	2,937	2,891	3,156	3,468
Loan Funds	2683	2601	2027	1927	1827
Minority Interest	(2)	(1)	(1)	(1)	(1)
Deferred Tax Liabilities	77	157	255	255	255
Total Liabilities	5,377	5,695	5,172	5,337	5,549
Gross Block	3,036	3,809	3,721	3,921	4,121
Less:- Accumulated Depreciation	929	1,107	1,309	1,520	1,747
Net Block	2,107	2,702	2,413	2,401	2,374
Capital WIP	0	0	32	32	32
Net fixed assets	2,107	2,702	2,445	2,433	2,407
Investments	852	840	702	702	702
Inventory	927	786	596	653	736
Debtors	780	954	793	870	982
Loans & advances	196	399	559	581	605
Other Assets	59	93	120	120	120
Cash & bank balances	1,101	771	562	599	698
Total current assets	3,063	3,004	2,630	2,823	3,141
Trade payables	154	154	127	131	147
Other current Liab.	458	576	465	476	538
Provisions	35	121	13	14	16
Net current assets	2,416	2,153	2,025	2,202	2,440
Total	5,377	5,695	5,172	5,337	5,549

Source: Company, Centrum Research Estimates

Exhibit 9: Cash Flow

Y/E March (Rs.mn)	FY16	FY17	FY18	FY19E	FY20E
CF before WC changes	648	726	548	624	687
Working capital changes	312	243	(81)	(140)	(139)
Cash from Operations	832	856	378	320	369
Adj. OCF (OCF-Interest)	768	785	303	262	314
Capex	(369)	(773)	(145)	(200)	(200)
Adj. FCF (AOCF-Capex)	398	12	159	62	114
Cash from investing	(567)	(676)	172	(5)	15
Cash from financing	(104)	(512)	(758)	(278)	(285)
Net change in cash	161	(331)	(208)	37	99

Source: Company, Centrum Research Estimates

Appendix A

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Sarla Performance price chart



Source: Bloomberg, Centrum Research

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